CalPERS Infrastructure Policy – Comments from External Entities

CalPERS Infrastructure Policy	
	Responsible Contractor Policy - Section VI.E.1.
Comments from LIUNA March 2008	The real estate RCP application provisions state that the RCP will not apply to an investment or joint venture where CalPERS owns 50% or less. While understandable, this has led to problems in the past and the LIUNA led effort to establish "spirit" of the policy language where the agreement does not apply in practice. CalPERS added "spirit" language to its Real Estate RCP in 2005, but then rejected our attempts to define what that means (CalPERS advocating for responsible contractors, disclosure of project information, working to set up meetings with partners, etc.). • The above problem is worse with infrastructure investments. The size of such projects is normally much larger than the average real estate deal and joint ventures and consortiums are common – meaning that in many instances it is unlikely that CalPERS would ever have a clear 50% or greater ownership. Therefore, we have advocated that the application language be changed. There are several possible improvements that could be made: • Eliminate the joint venture language and 50% language, and then build in an "appeal/exceptions" clause where investment groups who object could make their case for waiver directly to the investment committee. (John Adler from SEIU suggested this on the call.) • Build in stronger "spirit" language as described above. • Only make investments with infrastructure products that have internally adopted the RCP currently in place at Alinda and Carlyle.
Comments from PECG March 2008	The policy statement (Section VI.E.1 - RCP) would apply that program to managers of any investment vehicle under consideration. That is most appropriate and should be adhered to. The responsible contractor program requires competitive bidding for contractors and subcontractors. PERS should not invest in any project which does not adhere to that policy. PERS should also be aware that typical PPP projects do not utilize competitive bidding. PECG and PERS staff have met and discussed this issue in some detail. Essentially, PPP projects have proven to be bad investments in the transportation field, resulting in doubling of costs which lead to taxpayer or other bailouts, primarily because of a lack of competitive bidding and the utilization of other unsound contracting practices.

CalPERS Infrastructure Policy	
Responsible Contractor Policy - Section VI.E.1. (continued)	
Comments from SEIU **March 2008**	We believe the responsible contractor policy (RCP) should apply to all CalPERS infrastructure investment vehicles, not only to direct investments as the real estate RCP does, for the following reasons: • The infrastructure asset class is just starting in the U.S., and CalPERS' insistence on responsible contractor policies will be influential in persuading investment managers to adopt and abide by them. This will send a clear market signal that labor risk associated with infrastructure investments must be addressed proactively. • As staff indicated during the conference call with stakeholders on January 31, 2008, a number of infrastructure managers have adopted responsible contractor policies which incorporate the principles embodied both in the Public Outsourcing Policy section and the responsible contractor policies. There is no reason for CalPERS to require compliance with the public outsourcing policy while not requiring compliance with responsible contractor policy; consistency requires compliance with both, which the market has shown will not diminish CalPERS' investment opportunities. In both cases, the policy would allow staff to recommend to the Investment Committee investing with a manager that does not agree to these policies—should there be no other way to satisfy fiduciary obligations. • There is no reason to incorporate the public outsourcing policy as a requirement for all managers while managers that have adopted responsible contractor policy are only given a "strong preference." We should keep the preference for managers that have adopted internal RCPs for all their investments while requiring all managers to agree to abide by RCP as a condition of CalPERS' investment, subject to the same waiver language incorporated for the public outsourcing policy. The "strong preference" language is <u>not</u> a substitute for an RCP compliance requirement. The RCP must apply to all types of investment vehicles, including those excluded for real estate investments under Section VI. A of the RCP.
Response from CalPERS Staff **March 2008**	**CalPERS is committed to the Responsible Contractor Program as it is has a long standing reputation for supporting and encouraging fair wages and benefits for workers. As such, CalPERS intends to work with third parties that have also implemented a policy regarding responsible contracting. In situations where CalPERS is a minority investor, CalPERS has stated its preference for working with third parties that are also committed to responsible contracting. This preference language can be found in Section VI. E. 3 of the policy.** **Any changes to the existing CalPERS Responsible Contractor Policy and its applicability would require a separate process outside of the Infrastructure Policy process. Changes to the RCP would need to be presented to the CalPERS Policy Subcommittee and Investment Committee for approval before they could be implemented.**

CalPERS Infrastructure Policy	
Responsible Contractor Policy - Section VI.E.1. (continued)	
Comments from LIUNA April 2008	We believe that much positive headway has been made and approve of the most recent changes. We do offer the following additional comments regarding Section VI.E (b) Preference. We believe that the language should be changed as follows: *"Preference. Staff shall give a strong preference to all infrastructure investment vehicles that have adopted an internal policy regarding responsible contracting consistent with the CalPERS Responsible Contracting Policy subject to the fiduciary conditions laid out in Section IV of the CalPERS Responsible Contracting Policy."* We make this proposal because the fiduciary standards for responsible contracting have already been laid out in detail in the current RCP (after much discussion over the years) and the infrastructure policy which uses that RCP as its basis should use the same standards. Using different fiduciary standards from policy to policy will cause confusion and inconsistency.
Comments from SEIU April 2008	This most recent draft does make some substantive improvements and we appreciate the consideration given to our comments. However, we do believe however that there are still some outstanding issues that would benefit from additional changes or discussion at the policy committee. We would like to clarify what the changes proposed imply here. As we read this, it is our understanding that all investment vehicles will need to either comply with the RCP (if applicable) or will need to adopt an internal policy that is at least as strong as the CalPERS policy in order to receive an investment recommendation. In the event that staff still wishes to go forward with the investment it must be brought forward for consideration by the Investment Committee. If this is correct we suggest the following clarifying language. We would also like it made clear that investment funds that have adopted and internal policy agree to maintain the policy for the life of the fund. Section VI.E.1.c This preference shall apply to any domestic infrastructure investment vehicle for which the RCP is not applicable by its terms other than to make a good faith effort to comply with the spirit of the policy. This specifically applies to investments including, but not limited to, commingled funds, opportunity funds, mezzanine debt, and hybrid debt investments. *"CalPERS shall obtain written confirmation that said policy will remain in force for the life of the vehicle."* Section VI.E.d If the manager of any investment vehicle does not agree to ~~adopt~~ *"comply with"* Sections VI(E)(1)(a) or adopt an internal policy regarding responsible contracting, and, if Staff deems it appropriate based on all the circumstances, including the intent of this Policy as well as the investment merits of the investment vehicle, Staff may recommend the potential investment to the Investment Committee and the Committee shall make a determination whether or not to invest in such investment vehicle.

CalPERS Infrastructure Policy	
Responsible Contractor Policy - Section VI.E.1. (continued)	
Response from CalPERS Staff **April 2008**	**The preference language that has been developed pertaining to responsible contracting policies is based on CalPERS' Responsible Contracting Policy that is in existence. Inherently this policy is subject to CalPERS' fiduciary duties and as such, the language within the Section VI.E.1.b has been revised to reflect that the policy is subject to fiduciary duties. The intent of the Responsible Contracting Policy section of the policy is to make domestic investment vehicles either comply with the RCP or to comply with an internal policy that is consistent with the RCP. Section VI.E.1.a clearly states that investment managers must provide written agreement pertaining to their adoption of responsible contracting policies.**

CalPERS Infrastructure Policy	
Domestic Public Sector Jobs - Section VI. E. 2.	
Comments from PECG **March 2008**	Section VI.E.2. states that a good faith effort will be made to ensure that no more than minimal public employee job loss and other potential adverse impacts on employees will occur. This is outrageous. A PERS policy to allow investment of PERS funds into a project which would result in any job loss or adverse impact on PERS members is totally unacceptable. The same is true of supposed good faith efforts to "minimize the impact of privatization on public sector employment". It would be a betrayal of the interests and the trust of the members of PERS if its retirement system used members' funds to result in job loss or other adverse impacts on PERS members. The only acceptable position to PECG and, no doubt, all PERS members is a policy which, without exception, prohibits investment in any project or program which would result in any job loss or adverse impacts on any PERS public employee members.
Comments from SEIU **March 2008**	We believe that the Domestic Public Sector outsourcing language should be strengthened further to make explicit the tension that exists between protecting plan participants jobs and making returns in public private partnerships. Page 4 paragraph E 2 (Section VI.E.2) Rather than implying that it is optional, we would like to see language that managers are strongly encouraged to (vs may) work directly with public employees. Further we believe that investments considered that will or could directly impact the jobs of CalPERS plan participants must be brought to the investment committee for approval.
Response from CalPERS Staff **March 2008**	**The language in Section VI.E.2 is intended to protect the interest of public sector employees to the maximum extent possible. Similar language has been negotiated and adopted by other labor constituents as well as some of the major funds pertaining to the loss of public employee jobs. While CalPERS may not be in a position of control with all of its investments, it can encourage all parties involved in an investment to make a best effort at minimizing the loss of public sector jobs. We have inserted language that the Investment Committee will also review any investment which could directly impact the jobs of CalPERS' plan participants.**

CalPERS Infrastructure Policy	
Domestic Public Sector Jobs - Section VI. E. 2.	
Comments from PECG April 2008	PECG opposes outsourcing of PERS member jobs or any adverse impact of PERS members. Unfortunately, while PERS staff has sought to address these issues in their proposed policy, they have written the policy in a manner which would allow a PERS investment vehicle to act contrary to the employment or other interest of PERS members. Such a policy, which would allow PERS to invest money in an manner contrary to the interest of its members, would be inexcusable. It should be obvious that engaging in an "investment activity" and "investment transaction" which could result in an actual or potential adverse impact on a member's employment or employment opportunity would be directly contrary to the constitutional, statutory, and policy obligations of CalPERS. This would be true whether the adverse impact was permitted by PERS policy or an actual investment by PERS. At our latest conference call meeting, a valid point was made regarding the impact on public employees. PERS does not represent all public sector employees. Therefore, it could be reasonable for a policy to make good faith efforts to minimize adverse impacts on public employees other than PERS members, while at the same time guaranteeing that PERS members would not be adversely impacted by an investment. Therefore, the draft policy recommended by PERS staff could be acceptable if it contained the following statement: "Regardless of any provisions in this or any other PERS policy, the investment vehicle for any infrastructure investment program shall insure that there will not be any actual or potential adverse employment or other impact of PERS members or participants." The intent of this wording is to ensure that, when PERS invests its members' funds, that investment shall not have any adverse impact on its members, now or in the future. We could discuss alternate wording to achieve this objective if you or the PERS Board of Administration wish to do so.
Comments from SEIU April 2008	We offer below some intent language (borrowed largely from the AIM outsourcing policy) to provide appropriate context for this section. We believe strongly that CalPERS should affirmatively and proactively seek out managers who understand that to the greatest extent possible their investments should seek to bolster not harm the public sector and public services. Upon discussion with our members we also urge that all funds that would affect public sector jobs in California be brought to the Investment committee, and that transactions that may affect CalPERS participants receive special protection during the life of any investment vehicle. Section VI.E.2 *"CalPERS is funded by and depends upon a healthy public sector. Investments in infrastructure may involve unique risks related to the potential outsourcing of public sector work. Outsourcers may be exposed to political resistance, labor disputes and public relations risks. In addition, the outsourcing of public sector jobs may cause public sector workers, including CalPERS members, to be laid off and be offered new private sector jobs in which they perform the same work but with inferior wages, benefits or working conditions. Consistent with our objective of being responsible stewards, CalPERS will seek out investment vehicles that aim to bolster and enhance the health of the public sector and public sector employment rather than to harm or diminish public sector jobs or the quality of public services."*

CalPERS Infrastructure Policy	
	Domestic Public Sector Jobs - Section VI. E. 2. (continued)
Comments from SEIU April 2008	Staff will also present to the Investment Committee for consideration any investment that would directly impact the jobs of ~~CalPERS' plan participants~~ *"California public sector workers. In the event that any investment vehicle to which CalPERS has committed becomes involved in a transaction that may impact CalPERS participant jobs, the managers of this vehicle will report to the Investment Committee prior to closing of said transaction on the efforts planned or already taken to comply with this policy."*
Response from CalPERS Staff April 2008	**This issue of protecting public sector jobs is a high priority and staff recognizes the overall sensitivity to this issue and others within the context of the infrastructure policy. Staff has attempted to draft language that protects workers. We would like to give CalPERS board members the opportunity to review and opine on the infrastructure policy so as to provide the appropriate feedback regarding this topic.** **CalPERS has a fiduciary duty to seek out investment vehicles that meet and exceed numerous standards. When looking at investment vehicles Staff must take into consideration a myriad of things including, but not limited to, investment track record, risk analysis, due diligence, responsible contracting, outsourcing, portfolio allocation, risks and returns, etc.**

CalPERS Infrastructure Policy	
Other Considerations - Section VI. E. 4.	
Comments from PECG **March 2008**	Section VI.E.4. (Other Considerations Regarding the RCP and POP) is also unacceptable. It says if the investment vehicle manager won't agree to the policies stated above, PERS staff can still recommend that the Investment Committee approve the investment. Thus, PERS would invest its members' funds in a project which did not utilize responsible contractor practices (such as competitive bidding) and could result in more than minimal job loss by PERS members!
Response from CalPERS Staff **March 2008**	**If the CalPERS staff has reviewed an investment whereby certain policies have not been adopted, and the staff is still interested in pursuing the investment given that other aspects of the investment are aligned with investment parameters and expectations, the staff will have to present the investment to the Investment Committee at which point the CalPERS Investment Committee will make the final decision about the opportunity. The Investment Committee will also review any investment which could directly impact the jobs of CalPERS' plan participants.**
Due Diligence - Section VIII.A.3	
Comments from SEIU **March 2008**	An analysis of labor risk in particular investments really should include a complete understanding of the labor context—and as such relevant labor union representatives should be consulted as a routine part of due diligence. The annual report on the portfolio should include an ongoing evaluation of labor and political risk exposures as well as reporting on this area related to the industry as a whole. Specifically, the report should include for each investment vehicle the number and type, nature and compensation of jobs created, jobs transferred from public sector to private sector, and jobs retained in the public sector.
Response from CalPERS Staff **March 2008**	Labor risk is noted as an investment risk within the Infrastructure Policy. In addition, when needed, staff may contact the necessary labor representatives, as well as other resources, to explore specific topics and issues. Under Section VIII.B.4 we have added the following due diligence item pertaining to labor: ***"Review and analysis of ownership structure, employee benefit plans, anti-takeover provisions, labor contracts; and as appropriate, consultation with relevant labor representatives."***

CalPERS Infrastructure Policy	
Other Comments	
Comments from CERES/Investor Network March 2008	In Section II. Strategic Objectives add to G: G . Act as a responsible steward of Program investments through quality services, responsible labor practices, and a commitment to environmental sustainability, affordability and accessibility. In Section VI. Investment Approaches and Parameters add a new section: E. Consideration of Environmental Sustainability Factors: It is the intent of this policy that in evaluating proposed partnership, direct investment, and strategic investment vehicle opportunities, Staff and where appropriate, the Investment Committee will consider the environmental sustainability of the investments with particular concern for the investment's energy efficiency, adherence to smart growth principles, fuel economy, and alternative energy generation and distribution impacts. And under Risk Parameters, add: "Climate Risk: In the current carbon constrained economy, long term investment returns may be impacted by risks and opportunities related to climate change."
Response from CalPERS Staff March 2008	**CalPERS is committed to addressing environmental issues and is interested in addressing the impacts of infrastructure assets on the environment.** **Section II. G has been updated to state the following: "Act as a responsible steward of Program investments through quality services, responsible labor and management practices and responsible environmental practices." Under Section VI.M. Renewable Energy and Sustainability, language has been added which addresses environmental issues. Under Section VI.K a risk parameter addresses climate risk.**
Comments from CERES/Investor Network April 2008	You have captured our essential concern that infrastructure investments will, by their nature, have impacts on the environment. We appreciate your willingness to incorporate this "big picture" view into the policy as well as squarely address climate and environmental risk as one of your risk parameters. This Cal PERS policy is one of the first investment policies for this type of asset. Ceres will point other funds in the Investor Network for Climate Risk to this policy as good model as it appropriately considers both the traditional risks and opportunities and the ever more significant climate risks and opportunities as part of the investment decision process. Thank you for all of your work on this. It has been an easy drafting process. We look forward to its passage at the Board and the potential for us all to learn from your investment experience as the program unfolds.

CalPERS Infrastructure Policy	
	Reporting – Section IX.A.4
Comments from SEIU April 2008	We have also added a suggestion regarding reporting on the impact of both of these programs within the context of the responsible stewardship strategic objective. Quarterly and annual reports shall be provided to the Investment Committee. These reports shall include reviews of investments ~~and~~ their performance *"and progress relative to all strategic objectives of the asset class. With regard to strategic objective II G, the report shall include a review of public services provided, employment (public v private sector job loss or growth, geographic distribution etc…) and environmental impacts (beneficial as well as negative) associated with current investments."*
Response from CalPERS Staff	**On a quarterly and annual basis reports will be provided to the investment committee which will address the performance of investments as well as overall progress relative to all strategic objectives and not just one strategic objective which has been referenced.**

CalPERS Infrastructure Policy	
Other	
Comments from AFSCME March 2008	Responsible infrastructure investment opportunities available to CALPERS include: • Direct long-term loans • Monetization of future revenue streams • Long-term leases with public agency operating agreements • Direct investment or co-investment with public or nonprofit agencies These investments can offer CALPERS long-term predictable returns based on stable cash flows. These arrangements should be of interest to publicly-owned and operated utilities (water, sewer, electric, gas) and toll/revenue generating transportation entities. Financing might also be used to support innovative municipal-based residential and commercial energy conservation investments. CALPERS should match these qualities of inflation linked assets to prioritize its investments in a way that replaces and rehabilitates existing infrastructure that will improve the quality of public services, reduce operational costs and strengthen the local economic base while being environmentally responsible. We encourage CALPERS to engage directly with the public owners of infrastructure, rather than participating in investment pools controlled by investors seeking the high alpha with correspondingly high betas, which also characteristically are managed without regard to the social consequences for infrastructure users, workers and communities. To insure the long-term viability and public acceptance of its investments, CALPERS should require as a condition of its investment that • The goals of the project and the financial implications for individual users be clearly communicated; • Local financing decisions are based on a comprehensive and transparent review of alternatives; • An analysis is undertaken to insure that the investment is affordable to the community and the individual users of the infrastructure; • Stakeholders, including all responsible elected officials, have sufficient time to review the proposal prior to commitment; • Binding commitments to maintain and service the infrastructure are included in any agreements; • Public employees' employment, wages, benefits, pensions and union rights are protected through enforceable provisions; and, • The public agency has the capacity to manage the development, operation and maintenance of the project. Under these conditions CALPERS infrastructure investments will protect the pensions of its public employee members, strengthen the economic health of their communities and protect the public interest.

CalPERS Infrastructure Policy	
Other (continued)	
Response from CalPERS Staff March 2008	There are vast investment opportunities within infrastructure available to CalPERS. The infrastructure policy as proposed anticipates that CalPERS will make investments in both publicly owned (public private partnerships) as well as privately owned assets. It should be noted that the majority of infrastructure investments to date in the United States have been within the private sector. In addition the policy anticipates that investments will be made in different sectors including transportation, ports, energy, water, communications and social infrastructure. Infrastructure assets are long-lived assets which typically generate steady and predictable cash flows. They perform well during economic downturns and provide an inflation hedge. Infrastructure assets also have a low correlation to traditional asset classes and provide diversification in an investment portfolio. These equity investments generate attractive yields (up to the middle teens) but have a lower risk profile than other alternative asset classes. These qualities as well as the ability to assist with liability driven investments and provide duration hedging while facilitating essential services to the community make infrastructure investments interesting and attractive. The infrastructure policy as proposed allows CalPERS to invest in infrastructure via funds as well as direct investments. These methods of investment provide flexibility given limited staff resources and allows CalPERS time to further its expertise in the infrastructure sector. These methods of investment are also available in other CalPERS alternative asset classes. CalPERS is committed to responsible contracting principles and the protection of the interest of public employees and intends to work with third parties who also adhere to these goals.